

Message Text

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ACTION EB-07

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SUBJ: RASTRA BANK ESTIMATES LARGE DRAWDOWN
IN FOREIGN EXCHANGE

1. RASTRA BANK OFFICIALS ARE NOW IN PROCESS OF MAKING
PRELIMINARY ESTIMATES OF NEPAL'S FOREIGN EXCHANGE POSITION
FOR END OF NEPALESE FISCAL YEAR JULY 15. WHILE FINAL
FIGURES WILL NOTBE AVAILABLE UNTIL SEVERAL WEEKS AFTER
END OF FISCAL YEAR, PRESENT ESTIMATES INDICATE THAT
DRAWDOWNS OF CONVERTIBLE FOREIGN EXCHANGE COULD RANGE FROM
\$25 TO \$40 MILLION FROM LEVEL OF \$111 MILLION AT END OF
PREVIOUS FISCAL YEAR. SHOULD ALL PRESENTLY OUTSTANDING
ACCOUNTS CLEAR BY END OF FISCAL YEAR, NET DEFICIT IN
CONVERTIBLE CURRENCY ACCOUNT WOULD APPROXIMATE \$40 MILLION.
SHOULD SOME ACCOUNTS NOT CLEAR, GROSS DEFICIT WOULD
APPROXIMATE \$25 MILLION.

2. ESTIMATED NET DEFICIT OF \$40 MILLION COMPARES WITH
SURPLUS OF \$12 MILLION LAST YEAR. IF INDIAN CURRENCY
RESERVES ARE INCLUDED IN FOREIGN EXCHANGE HOLDINGS, RASTRA
BANK ESTIMATES THAT NET DEFICIT WILL APPROXIMATE \$35

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MILLION, AS BANK OFFICIALS ARE NOW ANTICIPATING A NET

SURPLUS OF \$5 MILLION IN IC TRANSACTIONS, COMPARED TO DEFICIT OF \$4 MILLION LAST YEAR.

3. WIDE SWING OF \$52 MILLION IN HOLDINGS OF CONVERTIBLE FOREIGN EXCHANGE RESERVES IS DUE TO SEVERAL FACTORS. AS RESULT OF SHORTAGE IN HOLDINGS OF INDIAN CURRENCY, STANDBY CREDIT WITH INDIAN GOVERNMENT FOR \$10 MILLION EQUIVALENT INDIAN RUPEES WAS REPAID IN DOLLARS. BOTH QUANTITY AND PRICE OF IMPORTS ARE UP SIGNIFICANTLY COMPARED TO PREVIOUS YEARS, AND GON HAS ADOPTED POLICY OF SWITCHING SOURCE OF SUPPLY FOR SOME COMMODITIES FROM INDIA TO THIRD COUNTRIES AS IS REFLECTED BY MARKED INCREASE IN DRAWDOWNS OF CONVERTIBLE FOREIGN EXCHANGE AND SURPLUS IN IC ACCOUNT.

4. HIGHER LEVEL OF IMPORTS AT INCREASED PRICES HAS LED TO PROBLEM IN DISPOSITION OF SOME DEVELOPMENT GOODS. WITH PRICE OF SOME COMMODITIES SUCH AS CEMENT HAVING INCREASED SHARPLY, PROJECTS WITH FIXED BUDGETS HAVE NOT BEEN ABLE TO TAKE DELIVERY OF ALL COMMODITIES PREVIOUSLY ORDERED. AS RESULT GOVERNMENT CORPORATIONS SUCH AS NATIONAL TRADING ARE ENGAGED IN FRANTIC SEARCH FOR WAREHOUSE SPACE WHERE GOODS CAN BE STORED UNTIL AGENCIES ORDERING GOODS CAN COME UP WITH FUNDS REQUIRED FOR PAYMENT.

5. GON ESTIMATES ON FOREIGN EXCHANGE HOLDING ARE BASED ON ASSUMPTION THAT RICE TRADE WITH INDIA WILL FINISH YEAR AT SATISFACTORY LEVEL. GON IS ATTEMPTING TO EXPORT INCREASING QUANTITIES OF ITS RICE TO STATES IN SOUTHERN INDIA WHERE PRICE IS HIGH, BUT HAS BEEN FRUSTRATED IN ITS EFFORTS TO DATE BY GOVERNMENTS OF BIHAR AND UP WHICH LIMIT TRANSIT PERMITS FOR NEPALESE RICE ENROUTE SOUTH TO 500 METRIC TONS AT ONE TIME. GON HOPES TO BE ABLE TO INCREASE LIMIT TO 10,000 METRIC TON LOTS, WHICH WOULD ENABLE IT TO MEET ITS RICE EXPORT OBJECTIVES. FOOD OFFICIALS FROM INDIAN GOVERNMENT ARE NOW IN KATHMANDU, INCLUDING REPRESENTATIVES FROM KERALA AND TAMIL NADU, AND NEPALESE HOPE THAT PROBLEMS CAN BE RESOLVED WITHIN NEXT TWO WEEKS.

6. COMMENT: AS GOVERNMENT STATISTICS ON FOREIGN TRADE WITH THIRD COUNTRIES AND FOREIGN EXCHANGE ACCOUNTS ARE LIMITED OFFICIAL USE

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ONLY ISSUED WITH SEVERAL MONTHS' LAG, WE ARE UNABLE TO CORROBORATE RASTRA BANK ESTIMATES. A DRAWDOWN OF \$40 MILLION WOULD TAKE A SIZABLE CHUNK OUT OF NEPAL'S HOLDINGS OF CONVERTIBLE FOREIGN EXCHANGE, WHICH TOTALED \$111 MILLION AT END OF PREVIOUS FISCAL YEAR, AND WOULD REPRESENT SHARP INCREASE IN RATE OF DRAWDOWNS DURING LAST SEVERAL MONTHS OF FISCAL YEAR AS CONVERTIBLE RESERVES IN MID-JANUARY TOTALED \$106 MILLION. (WE ARE ALSO UNSURE OF DWTENT TO WHICH

CORONATION MIGHT HAVE RESULTED IN INCREASED FOREIGN EXCHANGE EXPENDITURES.) WHILE EARLIER ESTIMATES HAD INDICATED NEPAL MIGHT ENCOUNTER SERIOUS BALANCE OF PAYMENTS PROBLEM IN FOUR TO FIVE YEAR, PRESENT ESTIMATES SIGNIFICANTLY ADVANCE TIME FRAME. CONTINUATION OF TREND WOULD DRASTICALLY ALTER NEPAL'S ECONOMIC FUTURE. RELATIVELY HIGH LEVEL OF FOREIGN EXCHANGE HOLDINGS HAD BEEN ONE OF PRINCIPAL FACTORS SEPARATING NEPAL FROM OTHER LDC'S. AS NEPAL WILL CONTINUE TO BE DEPENDENT ON IMPORTS TO SUPPORT ITS DEVELOPMENT AND AS ITS EXPORTS ARE LIMITED -- BASED PRIMARILY ON A DECLINING RICE SURPLUS -- BOTH THE GON AND FOREIGN AID DONORS MAY HAVE TO REORIENT THEIR PLANNING TO TAKE GREATER ACCOUNT OF BALANCE OF PAYMENT CONSIDERATIONS. QUANTON

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